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No. 91-1274

In the Supreme Court of the United States

OCTOBER TERM, 1991

LILLIAN WRIGHT, PETITIONER

v.

FEDERAL DEPOSIT INSURANCE CORPORATION, ETC.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether the court of appeals correctly applied the rule of *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942), and 12 U.S.C. 1823(e) to allow the FDIC to enforce promissory notes acquired as receiver of a failed bank, despite petitioner's affirmative defenses based on an unrecorded side agreement.

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OPINIONS BELOW

The opinion of the court of appeals, Pet. App. A1-A24, is reported at 942 F.2d 1089. The opinion of the district court, Pet. App. B1-B21, is unreported.

JURISDICTION

The judgment of the court of appeals was entered on August 29, 1991. The petition for a writ of certiorari was filed on November 27, 1991. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. On October 30, 1982, petitioner—then a director of Union National Bank, a federally insured national bank—executed two unconditional promissory notes payable to the bank for $75,200 and $25,000, respectively. Pet. App. B4-B5. The $75,200 note consolidated and renewed several prior notes that petitioner had previously signed and delivered to the bank. *Id.* at B7-B8. On November 12, 1982, petitioner executed a third unconditional promissory note for $27,000 payable to the bank. *Id.* at B5.

On July 8, 1983, the Comptroller of the Currency declared the bank insolvent and appointed the FDIC as receiver. Pet. App. B2. Petitioner's promissory notes were among the assets of the Bank acquired by the FDIC in its receivership capacity. The bank's records showed that petitioner had made no payments of the principal amounts owing on any of the notes. *Id.* at B7.

2. The FDIC sued petitioner in federal district court seeking to collect on the notes.[1] Petitioner admitted signing and delivering the notes to the bank, and stipulated that the notes were assets of the bank at the time the FDIC took over as receiver. Pet. App. A4. She asserted, however, that she had executed the $75,200 and $25,000 notes as part of an application for a line of credit, and that the bank had agreed not to enforce the notes unless it granted the loan application, which it never did. According to petitioner, no funds were ever advanced on the notes and thus they were invalid for lack of consideration. *Id.* at A5. Petitioner further claimed that she had repaid the $27,000 note. *Ibid.*

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[1] The FDIC also sued petitioner on two additional notes. Pet. App. B1-B2. Petitioner did not appeal from the judgments obtained by the FDIC on those notes.

The FDIC filed a motion in limine seeking to exclude any evidence in support of petitioner's defense of lack of consideration, relying on the common law estoppel rule established in *D'Oench, Duhme & Co.* v. *FDIC*, 315 U.S. 447 (1942), which forbids proof of secret side agreements that would defeat the FDIC's efforts to collect facially valid bank assets. The district court denied the motion, ruling that the *D'Oench* doctrine was inapplicable because the FDIC had failed to establish that petitioner's execution of the notes was part of a scheme or arrangement likely to mislead banking authorities. Pet. App. A4.

At trial, petitioner introduced a letter dated March 10, 1983, from the bank's president to petitioner. According to petitioner, the letter released her from any obligations on the $25,000 and $75,200 notes and indicated that the $27,000 note would be repaid from an escrow account. Pet. App. A5-A6.

The district court found for petitioner on all three notes. Pet. App. B1-B21. Even though the notes were "facially unqualified (albeit unsecured) unconditional promises to pay," *id.* at B5, the court concluded that the *D'Oench* doctrine was inapplicable because the FDIC had failed to demonstrate that the bank had carried the notes as assets at the time of the FDIC's takeover in July 1983. *Id.* at B17-B18. The court then found that the March 10, 1983, letter had cancelled the $75,200 and $25,000 notes. *Id.* at B7, B19-B20. The court also relied on the letter to conclude that the $27,000 note had been satisfied from an escrow account. *Id.* at B20.

3. The court of appeals reversed. Pet. App. A1-A24. The court held that the district court had "misapprehended the requirement of proving a scheme or agreement likely to mislead banking authorities" under the *D'Oench* doctrine, Pet. App. A17, and that *D'Oench* applies even in the absence of any intent to defraud. Pet.

App. A18. Thus, the court concluded that *D'Oench* and its statutory counterpart, 12 U.S.C. 1823(e),[2] barred petitioner's claim that the bank had agreed not to enforce the facially unconditional $25,000 and $75,200 notes. Pet. App. A19-A20.

The court of appeals also held that the district court erred in requiring the FDIC to prove that the $25,000 and $75,200 notes had been obtained from the bank's open files. Relying on testimony to the effect that the FDIC does not generally seek to enforce instruments found in a failed bank's closed files, and pointing to petitioner's stipulation that the notes were assets of the failed bank, the court held that the FDIC had met its burden of establishing an inference that the notes were valid assets of the bank. Pet. App. A20-A22, citing *FDIC* v. *Venture Contractors, Inc.*, 825 F.2d 143 (7th Cir. 1987).

The court of appeals next concluded that 12 U.S.C. 1823(e) barred petitioner's claim that, as set forth in the March 10 letter, the bank had agreed to accept funds from an escrow account in satisfaction of the $27,000

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[2] Section 1823(e) bars the assertion of an agreement against the FDIC to defeat or diminish the FDIC's interest in an asset unless the agreement meets each of four requirements: (1) it must be in writing; (2) it must have been executed by both the bank and the obligor contemporaneously with the acquisition of the asset by the failed bank; (3) it must have been approved by the bank's board of directors or loan committee and the approval must be reflected in the minutes of the board or committee; and (4) it must have been continuously maintained as an official bank record. Section 1823(e) was enacted in 1950 as a statutory counterpart of the *D'Oench* doctrine. See Act of Sept. 21, 1950, ch. 967, § 2, 64 Stat. 889. The original version of the statute applied only to the FDIC in its corporate capacity, but the statute was amended by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, § 217(4), 103 Stat. 256 (12 U.S.C. 1823(e) (Supp. I 1989)), to apply to the FDIC in its capacity as receiver as well. The court of appeals held that the 1989 amendment was applicable to petitioner's claims. Pet. App. A11-A16.

note. The court found that the agreement embodied in the March 10 letter was subject to Section 1823(e) because it tended to "diminish or defeat the" FDIC's interest in the note within the meaning of the statute. Since the letter failed three of the requirements of Section 1823(e)—it was not executed contemporaneously with the bank's acquisition of the note, it was not approved by the bank's board of directors or loan committee, and it had not been an official record of the bank continuously from the date of its execution—the letter could not be used to support petitioner's defense of accord and satisfaction. Pet. App. A22-A24.

ARGUMENT

The court of appeals' holding that petitioner's affirmative defenses are barred by the *D'Oench* doctrine and by Section 1823(e) is a correct application of settled law. The court's decision does not conflict with any decision of this Court or of any other court of appeals. Accordingly, further review by this Court is not warranted.

1. Petitioner first argues (Pet. 15-19) that the court of appeals' decision conflicts with decisions of other courts of appeals finding *D'Oench* and Section 1823(e) inapplicable where a note has been invalidated by acts independent of an unrecorded side agreement. The cases on which she relies, however, are inapposite. In *FDIC* v. *Bracero & Rivera, Inc.*, 895 F.2d 824 (1st Cir. 1990), the FDIC sought to enforce a mortgage note that had been paid and canceled before the FDIC took over as receiver; the district court expressly found that the bank records showing the note's cancellation and repayment "were in the hands of FDIC *at all relevant times*." *Id.* at 829 (emphasis by court of appeals). Thus, the court held that any "secret agreement" between the defendants and the bank was beside the point because the repayment and cancellation of the note "were independent of the alleged secret agreement." *Id.* at 830.

Similarly, in *Commerce Federal Savings Bank* v. *FDIC*, 872 F.2d 1240 (6th Cir. 1989), the FDIC sought to enforce a mortgage even though the bank's records clearly showed that the underlying debt had been repaid prior to the bank's failure, thus extinguishing the mortgage by operation of law. 872 F.2d at 1242 & n.3, 1244-1246. The mortgage contained a "dragnet clause" securing any subsequently incurred debts that came into existence prior to the satisfaction of the original debt, but the FDIC was unable to prove that any such debts existed. Thus, the Sixth Circuit held that the repayment of the original debt—an act independent of any side agreement and clearly reflected in the bank's records—extinguished the mortgage for purposes of Section 1823(e).[3]

In this case, by contrast, the bank's alleged promise not to enforce the $25,000 and $75,200 notes was itself a secret side agreement, and thus could not constitute a

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[3] *Grubb* v. *FDIC*, 868 F.2d 1151 (10th Cir. 1989), is of no assistance to petitioner. See Pet. 17. In *Grubb*, the district court had entered judgment denying the bank recovery on certain notes before the FDIC acquired the bank's assets. Noting that the district court's "judgment provided the FDIC a reliable record indicating that the notes were void," 868 F.2d at 1159, the court held that the FDIC had acquired no interest in the notes, and that Section 1823(e) and *D'Oench* were therefore inapplicable. *Grubb* is clearly distinguishable, because in this case the FDIC had no "reliable record" of the alleged side agreement canceling the notes.

Finally, petitioner's reliance (Pet. 16) on *dicta* in *FDIC* v. *Merchants National Bank*, 725 F.2d 634 (11th Cir.), cert. denied, 469 U.S. 829 (1984), is of no avail. That case holds that, in general, the only evidence that may be admitted to defeat a claim by the FDIC to collect a failed bank's asset is evidence meeting the strict requirements of Section 1823(e). See 725 F.2d at 639. This case does not fall within the "narrow exceptions" to Section 1823(e) noted in *Merchants National*, because petitioner's defenses are not based on "acts independent of any understanding or side agreement." *Ibid.*

valid defense against the FDIC. There is simply no factual basis for petitioner's claim (Pet. 16) that the alleged cancellation of her promissory notes was an act independent of that undisclosed side agreement. Neither the notes she executed, nor the bank's official records, revealed any conditions on repayment of the notes.[4] The court of appeals' decision is fully consistent with this Court's decisions in *D'Oench* and *Langley* v. *FDIC*, 484 U.S. 86 (1987), as well as decisions of other courts of appeals that have consistently applied *D'Oench* and Section 1823(e) to protect the FDIC from a defense of lack of consideration. See, *e.g.*, *FDIC* v. *Caporale*, 931 F.2d 1, 2 (1st Cir. 1991); *FDIC* v. *McCullough*, 911 F.2d 593, 601 (11th Cir. 1990), cert. denied, 111 S. Ct. 2235 (1991); *FDIC* v. *McClanahan*, 795 F.2d 512, 515-516 (5th Cir. 1986).

Similarly lacking in merit is petitioner's assertion (Pet. 18) that Section 1823(e) does not apply to her defense that the March 10 letter shows satisfaction of the $27,000 note. The court of appeals' decision on that issue is fully consistent with the decisions of other circuits applying Section 1823(e) to exclude accord and satisfaction defenses based on written side agreements. See, *e.g.*, *FDIC* v. *Manatt*, 922 F.2d 486, 488-489 (8th Cir.), cert. denied, 111 S. Ct. 2889 (1991); *FDIC* v. *Rivera-Arroyo*, 907 F.2d 1233, 1236 (1st Cir. 1990). Moreover, the *D'Oench* doctrine compels the same result, because the March 10 letter constituted an unrecorded side agreement that was likely to mislead banking authorities. See, *e.g.*, *Savers Fed. Sav. & Loan Ass'n* v. *Amberley*

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[4] Petitioner asserts (Pet. 22) that the notes were in fact facially qualified and conditional. The district court's findings to the contrary, Pet. App. B5, were not disturbed on appeal, however, and should be deemed conclusive. See *Goodman* v. *Lukens Steel Co.*, 482 U.S. 656, 665 (1987). Likewise, the court of appeals' fact-bound determination that the March 10 letter was not found in the bank's records, Pet. App. A23, is not worthy of review.

Huntsville, Ltd., 934 F.2d 1201, 1206-1207 (11th Cir. 1991) (*D'Oench* bars reliance on any written or unwritten side agreement that does not appear in the bank's records).[5]

2. Petitioner also contends (Pet. 19-27) that the application of *D'Oench* and Section 1823(e) to foreclose her defenses to the notes constitutes a violation of due process. There is no merit to that claim.

As this Court has observed, under the Due Process Clause government "remains free to create substantive defenses or immunities for use in adjudication." *Logan* v. *Zimmerman Brush Co.*, 455 U.S. 422, 432 (1982). The Clause generally forbids government to deprive persons of property interests without providing them an opportunity to be heard, *id.* at 433, but petitioner had ample opportunity to contest the applicability of *D'Oench* and Section 1823(e) to the facts of her case. Due process requires no more.[6]

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[5] Petitioner suggests in passing (Pet. 24 n.5) that the court of appeals erred in applying the amended version of Section 1823(e) to this case. That issue is irrelevant, however, because the *D'Oench* doctrine would compel the same result even if Section 1823(e) were inapplicable. *D'Oench* has consistently been applied in cases where the FDIC acted as receiver, see *Timberland Design, Inc.* v. *First Serv. Bank for Sav.*, 932 F.2d 46, 49 (1st Cir. 1991) (citing cases), and thus the 1989 extension of Section 1823(e) to the FDIC in its receivership capacity merely restated existing law, see *Twin Constr., Inc.* v. *Boca Raton, Inc.*, 925 F.2d 378, 382 & n.2 (11th Cir. 1991); *FDIC* v. *State Bank*, 893 F.2d 139, 143 (7th Cir. 1990).

[6] The courts of appeals have uniformly rejected similar due process challenges. See, *e.g.*, *Campbell Leasing, Inc.* v. *FDIC*, 901 F.2d 1244, 1248 (5th Cir. 1990); *FDIC* v. *State Bank*, 893 F.2d 139, 144 (7th Cir. 1990); *Chatham Ventures, Inc.* v. *FDIC*, 651 F.2d 355, 362-363 (5th Cir. 1981), cert. denied, 456 U.S. 972 (1982).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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